

Attachment A

Alaska Communications Systems

3Q Results Show Improvement, We Remain Cautious

Alaska Communications Systems

Ticker	ALSK	EPS	2002E (Old)	2002E (New)	2003E
Price(10/24/02)	\$2.45	1Q (Apr)	(\$0.01)A	(\$0.01)A	
52-Wk.Range	\$1.48-8.28	2Q (Jul)	\$0.13A	\$0.13A	
Mkt.Cap(MM)	\$77.55	3Q (Oct)	(\$0.11)	(\$0.22)A	
Fiscal Year	Jan	4Q (Jan)	(\$0.11)	(\$0.11)	
Shares O/S(MM)	31.65	FY	(\$0.10)	(\$0.20)	(\$0.25)
		Revenue FY	\$330.83	\$333.10	\$340.00
		(MM)			

Underweight

- ACS's third quarter results show improvement from the dismal second quarter, but are still below historical trends
- Results from the State of Alaska contract and the cellular segment mitigate local telephone line losses
- We believe the company's near-term upside potential remains low

US Wireline Services:
Marc Crossman
(1-212) 622-6477
marc.crossman@jpmorgan.com
Steven J. O'Brien
(1-212) 622-6554
steven.obrien@jpmorgan.com

Sequential improvement in revenue and EBITDA did not bring ACS back to historic levels. ACS posted total revenue of \$84 million this quarter, up 3.6% from last quarter's recurring revenue, and 1.8% from third quarter 2001. Traditionally, the third quarter is one of the strongest quarters for ACS due to the better weather conditions and tourist season. Despite this, ACS's local telephone, directory, and interexchange segments did not bounce back from the previous quarter's weak results, remaining flat on a sequential basis. ACS's EBITDA margin of 36% this quarter was more than 3 percentage points better than last quarter; yet it remains well below the near 40% margins the company reported in the past. While we view overall results as a recovery from last quarter's disappointment, we would need to see growth rates and margins return to historical levels, in all segments, in order to justify valuation expansion.

State of Alaska and cellular performance mitigate the continued weak results of the local telephone segment. ACS posted strong cellular results this quarter. A relatively high ARPU of \$49 and growth in the net customer base drove strong sequential, and more importantly, year over year growth. ACS also met its forecast and exceeded \$3 million in State of Alaska contract revenue this quarter. We expect the company will need to continue producing strong results from these sources in order to counteract continued erosion of its local telephone business.

At current levels we do not see a compelling valuation upside. At its current price, \$2.45, we estimate ACS trades at roughly 5.2 times enterprise value to 2003 EBITDA. The Bells also trade in the low 5 times enterprise value to 2003 EBITDA range. ACS is experiencing competitive access line loss at a faster rate than the Bells. While cellular and State of Alaska results were positive this quarter, we do not believe ACS deserves at premium to the Bells at this time.

Alaska Communications Systems(ALSK/\$2.45/Underweight)

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October 25, 2002

Earnings Update

Company Rating:

Sector Weighting:

Market Weight

Telecommunications Services

ALSK-OTC (10/24/02)	\$3.51
12-18 mo. Price Target	\$5.00
Key Indices: None	
3-5-Yr. EPS Gr. Rate (E):	NM
52-week Range	\$9.81-\$2.47
Shares Outstanding	32M
Float	9.7M shrs
Avg. Daily Trading Vol.	NA
Market Capitalization	\$112.3M
Dividend/Yield	Nil/Nil
Fiscal Year Ends	December
Book Value	6.60 per Shr
2002 ROE	NM
LT Debt	\$610.00M
Preferred	Nil
Common Equity	\$187.80M
Convertible Available	No

Company Description

Alaska Communications Systems Group is a facilities-based carrier with a 500 mile fiber-optic network and 320,000 access lines. The company provides wireless, long-distance, and Internet access.

Cannon Carr
1 (212) 667-8129
Cannon.Carr@us.cibc.com

Gregor Dannacher, CFA
1 (212) 667-7049
Gregor.Dannacher@us.cibc.com

Joseph Altobello, CFA
1 (212) 667-8085
Joseph.Altobello@us.cibc.com

Alaska Communications

3Q Meets Revised Targets; Growth Ramp Still Uncertain

- ACS reported \$84M in revenue (2% growth) and \$31M in EBITDA (down YOY) for 3Q, in line with revised guidance after a disappointing 2Q. The company continues to face a challenging regulatory environment and competitive situation, which limit growth for the foreseeable future.
- The state contract, a key to long term growth, is finally generating revenue (perhaps \$1M per month), which hopefully ramps to \$1.5M or more per month early next year. We would hope to see better growth during 2H03 but that appears aggressive at this point.
- While line losses to GCI appear to have stabilized since 1Q02, the on-going reduction in lines continues to impede growth, particularly on access minutes. The company continues to work with state regulators to raise UNE rates but relief appears a year away.
- We remain cautious on ALSK. Management took an important first step this quarter by hitting initial cost cutting targets and billing for the state contract. Nevertheless, it will likely take several quarters to drive revenue growth and profitability.

Earnings per Share	Prev	Current
2000A		(\$0.44A)
2001A		(\$0.36A)
2002E		(\$0.39E)
P/E		
2000A		NM
2001A		NM
2002E		NM

Stock Price Performance



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Discussion

ACS reported \$84M in consolidated revenue and \$31M in EBITDA, both in line with our revised projections after a disappointing 2Q. ACS's results underscore the difficult market ACS faces—a regulatory regime that has set some of the lowest UNE rates in the US, an aggressive competitor in wireline, and challenging growth opportunities. ACS continues to lose access lines to competitor GCI (although it appears losses have stabilized), which in turn means lower access minutes, while new growth initiatives take time to ramp up. The company is actively working with regulators to increase the costs to lease loops, but the rate case decision is still probably one year away.

As we pointed out in 2Q, we believe the company is doing the right things in the interim: focusing on cost reduction (cost savings reportedly began this quarter, ultimately yielding \$6M annually in work force reductions by 4Q) and customer retention, marketing service bundles, and pursuing longer-term contracts more aggressively. It will take time for these initiatives to gain traction. Moreover, the company appears to be getting its state of Alaska contract up and running at this point, contributing about \$3M this quarter and perhaps \$4.5M per quarter starting next year. We had hoped for a more aggressive ramp-up (perhaps \$6-\$7M per qtr) because this is the key growth initiative for the company. Over time, we do expect each of these efforts to yield better stability in the customer base as well as drive new revenue opportunities, although this is difficult to model. Under current assumptions, it appears consolidated growth over the next 5-6 quarters will be disappointing, perhaps flat to slightly down initially but gradually ramping to a 3-4% growth rate by YE03.

The bright spot continues to be wireless, with revenue up 8% for the quarter and EBITDA margins a solid 40%. This helped to partially offset declines in data/Internet, where the company continues to incur up-front costs implementing the state contract.

Our price target of \$5 is based on relative valuations for incumbents, as well as the slower growth prospect near term. We assign a 5X multiple to 2002E ILEC EBITDA, a 7X multiple to wireless, and 7X multiple to directories, offset by \$585M in net debt. Risks to the company meeting our price target include a slower ramp in revenue and profitability in the Alaska contract, further share losses to aggressive competitors in wireline and wireless, and inefficient management of costs.

Our EPS estimates are shown below:

	1 Qtr.	2 Qtr.	3 Qtr.	4 Qtr.	Yearly
2000A Actual	(\$0.10A)	(\$0.08A)	(\$0.10A)	(\$0.16A)	(\$0.44A)
2001A Current	(\$0.15A)	(\$0.09A)	(\$0.04A)	(\$0.07A)	(\$0.36A)
2002E Current	(\$0.01A)	\$0.11A	(\$0.08E)	(\$0.08E)	(\$0.39E)

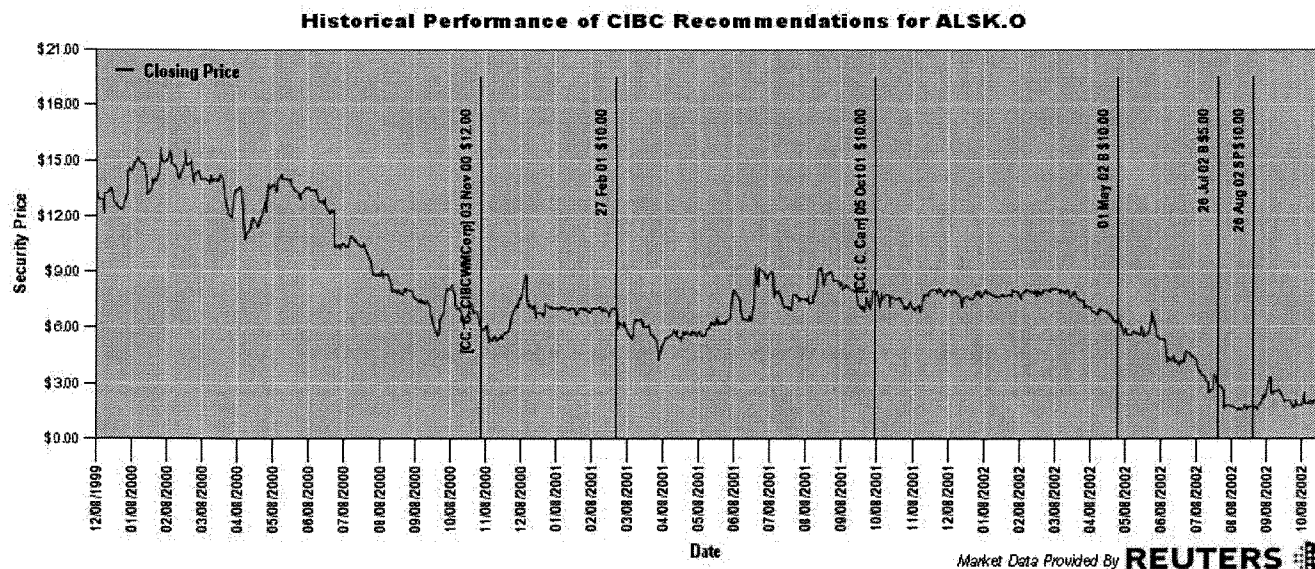
Companies Mentioned In This Report

Stock Prices as of 10/24/02:

General Communications (GNCMA-NYSE \$4.23 Not Rated)

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CIBCWM Price Chart**CIBCWM Stock Rating System**

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SP	Sector Performer	Stock is expected to perform in line with the sector during the next 12-18 months.
SU	Sector Underperformer	Stock is expected to underperform the sector during the next 12-18 months.
S	Suspended	Stock coverage is temporarily halted.
DR	Dropped	Stock coverage is discontinued.
NR	Not Rated	Stock is not covered by CIBCWM.
Company Ratings Prior To August 26th 2002		
SB	Strong Buy	Expected total return over 12 months of at least 25%.
B	Buy	Expected total return over 12 months of at least 15%.
H	Hold	Expected total return over 12 months of at least 0%-15%.
UP	Underperform	Expected negative total return over 12 months.
Sector Weightings**		
O	Overweight	Sector is expected to outperform the broader market averages.
M	Market Weight	Sector is expected to equal the performance of the broader market averages.
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NA	None	Sector rating is not applicable.

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Sector Outperformer (Buy)	257	34.8%	Sector Outperformer (Buy)	139	54.1%
Sector Performer (Hold/Neutral)	304	41.2%	Sector Performer (Hold/Neutral)	96	31.6%
Sector Underperformer (Sell)	177	24.0%	Sector Underperformer (Sell)	49	27.7%

Ratings Distribution: Telecommunications Services Coverage Universe

(as of 25 Oct 2002)	Count	Percent	Inv. Banking Relationships	Count	Percent
Sector Outperformer (Buy)	10	33.3%	Sector Outperformer (Buy)	6	60.0%
Sector Performer (Hold/Neutral)	9	30.0%	Sector Performer (Hold/Neutral)	4	44.4%
Sector Underperformer (Sell)	11	36.7%	Sector Underperformer (Sell)	3	27.3%

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Telecom Services Group

Update – October 25, 2002

Richard G. Klugman, CFA (212) 284-2031 rklugman@jefco.com

William Cook (212) 284-2566

wcook@jefco.com

Alaska Communications

NASDAQ: ALSK - \$2.45

Rating: Hold

Target Price	N/A	FY Dec	2001	2002E	2003E
52-Week Range	\$1-\$8	1Q	(0.14)	(0.01)	NA
Equity Market Capitalization	78	2Q	(0.07)	(0.20)	NA
Net Debt	576	3Q	(0.03)	(0.16)	NA
Total Enterprise Value	654	4Q	(0.06)	(0.15)E	NA
Shares Out (MM)	32	EPS	(0.30)	(0.52)E	(0.22)E
Avg Daily Vol (000)	29	P/E	NM	NM	NM
Annual Dividend	\$0.00	EBITDA	129	129	131
Dividend Yield	0.0%	TEV/EBITDA	5.1x	5.1x	5.0x
(\$MM, except per share data)		Revenue	331	342	345
(EPS on a recurring basis)		TEV/Revenue	2.0x	1.9x	1.9x

3Q Margins Ahead, Adjusting Estimates

We rate Alaska Communications Systems' shares **Hold**. Yesterday evening (October 24th), Alaska Communications reported third quarter earnings that were above our estimates for EBITDA (driven by recent cost-cutting efforts), but fell short of our EPS estimate on higher than expected depreciation expense (due to \$2 million of accelerated depreciation in the quarter, \$1.4 million of which was an out of period adjustment). We are tweaking our full year 2002 EPS estimate down to a loss of \$0.52 from a \$0.46 loss. We are also adjusting our 2003 EPS estimate to a \$0.22 loss from a \$0.25 loss as we expect cost-cutting measures to continue to improve margins, more than offsetting slightly higher depreciation expense.

- **Recurring EPS totaled a loss of \$0.16**, below the \$0.12 loss we expected, due to higher depreciation expense, which offset better-than-expected margins. Reported EPS was a loss of \$0.22, reflecting \$0.06 of losses on the disposal of assets related to the company's previously announced restructuring efforts.
- **Revenue grew 2% to \$84.3 million**, up from the normalized slight decline in the prior quarter and in-line with our \$84.2 million estimate and company guidance of \$83-\$84 million. Wireless revenue increased 4% in the seasonally strong third quarter, while the telco continued to post sluggish revenue trends, declining 2% (albeit better than the 3% decline we expected). Revenues from the new State of Alaska contract increased to \$3 million from the \$0.7 million posted in 2Q. Management expects to reach the \$4.5 million run-rate level by the end of the 4Q, as lingering customer billing issues are resolved.
- **EBITDA margin totaled 37%**, above our 35% estimate and up from the normalized 33% margin in the prior quarter (though still below the recent historical range of 38-41%) as the recent cost cutting initiatives were offset somewhat by weakness in the higher-margin telco business and start up costs related to the State contract.
- **Access lines declined for the third consecutive quarter, down 1.8%** - substantially worse than the slight (0.3%) decline in 2Q. Retail lines accounted for only 74% of total lines down from 75% in the prior quarter and 80% a year ago as competitors (especially GCI) continue to capture market share, primarily with UNE loops. While market share losses appear to have stabilized in Anchorage, GCI has expanded to Fairbanks and Juneau and is more actively taking share in those smaller cities, as expected.

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- **3Q wireless results were solid**, with the company adding 500 subscribers (slightly below our expectations) and revenue per subscriber increased 1% (as expected) as the warm late summer months drove customer usage.
- **The company added 1,200 DSL subscribers**, below our estimate of 1,500 additions, decelerating from results in the past 2 quarters.

Investment Conclusion

We rate Alaska Communications' shares **Hold**, noting the relatively high level of competition facing the company, its high leverage ratio (4.5x 2002 EBITDA), and the tough state regulatory environment. Alaska's shares trade at 5x 2003 EBITDA, at the bottom of the 5-6x range of the incumbent telcos (including RBOCs). In our opinion, this discount is warranted, given the aforementioned competitive, regulatory and financial pressure. We note that the company currently shows the weakest cash flow trends within its peer group and, following four consecutive quarters of modestly positive free cash flow, posted its second consecutive quarter of negative free cash flow in 3Q.

With its new data network built for the State of Alaska contract, the company could help its cause with additional data service contract wins (having already signed up Williams Petroleum.) However, we suspect such wins might not prove enough to offset growing difficulties in the core business.

Alaska Communications Selected Performance Data

	<u>3Q01</u>	<u>4Q01</u>	<u>1Q01</u>	<u>2Q02</u>	(Actual) <u>3Q02A</u>	(Est.) <u>3Q02E</u>
Recurring EPS	(0.03)	(0.06)	(0.01)	(0.20)	(0.16)	(0.12)
Reported EPS	(0.04)	(0.07)	(3.55)	(0.11)	(0.22)	(0.17)
Revenue growth	10.7%	8.6%	0.8%	13.5%	1.6%	1.9%
EBITDA margin	40.6%	38.3%	39.6%	38.6%	36.5%	34.5%
Telco line growth	1.3%	1.1%	-0.5%	-0.3%	-1.8%	-0.3%
Retail % of line	79.9%	78.4%	76.3%	74.9%	73.8%	73.8%
Wireless sub adds (000s)	0.2	1.4	(0.5)	1.5	0.5	0.6
Wireless rev/sub (% change)	-2.5%	-7.8%	-7.5%	0.0%	0.7%	0.5%
DSL sub adds (000s)	0.8	1.0	1.5	1.4	1.2	1.5

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- market capitalization - maturity - growth/value

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Risks that may impede the achievement of our Price Target include:

A decline in general economic conditions; Adverse news or other adverse events at another company in the sector; Unexpected news releases or management turnover; More restrictive governmental or environmental regulations; Disruption in materials from suppliers; Revenue short fall; Slow down in sales; Quarterly earnings decline; Inadequate cash flow to fund current operations.

Distribution of Ratings

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	% Companies Covered	% Banking Clients
Buy	67	15
Hold/Neutral	31	3
Sell	2	16

Price Chart(s)

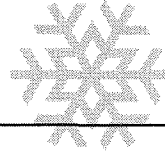
Price charts can be found on our web site at www.jefco.com.

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Equity Research

THE RLEC MONITOR



Winter



Legg Mason Telecom

Michael J. Balhoff, CFA
Christopher C. King
Bradley P. Williams

National Exchange Carrier Association

Victor S. Glass, Ph.D.

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.com

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For applicable current disclosures for all covered companies please write to the Legg Mason Research Department at the following address.

Legg Mason Research Department
Legg Mason Wood Walker, Incorporated
100 Light Street
P. O. Box 1476
Baltimore, Md. 21203-1476



Equity Research

Industry Update

The RLEC Monitor Winter 2003

TELECOMMUNICATIONS SECTOR

- As in previous editions, our RLEC Monitor provides an extensive view of rural local exchange carrier (RLEC) valuations, regulation, stock performance metrics, and other measures.
- We publish for the first time a primer on key upcoming regulatory rulings that will impact the RLEC industry in the next year, along with updated information on the amount of universal service subsidies received by each of companies covered in the Monitor.
- We are pleased to continue providing commentary from Dr. Victor Glass of The National Exchange Carrier Association (NECA), reflecting in this Monitor on NECA's recent rural end-user study, increasing pressure on the federal Universal Service fund and the impact of wireless services on rural carriers.
- Merger and acquisition activity in the RLEC space has declined since our Winter 2002 Monitor, as the capital markets have severely punished the overall telecommunications sector; however, we note that rural stocks in the Legg Mason RLEC Index have outperformed the regional Bell operating companies (RBOCs), the interexchange carriers (long-distance providers, or IXC), and wireless carriers over the past 12 months.
- Despite the weakened performance of telecommunications equities over the past year, the stocks of RLEC companies continue to be steeply undervalued on an asset valuation basis.
- We have a Buy rating on the shares of rural carriers CenturyTel, Inc. (CTL), Citizens Communications Company (CZN), and Commonwealth Telephone Enterprises (CTCO), and a Hold rating on the shares of Alaska Communications Systems (ALSK), Alltel Corporation (AT) and CT Communications (CTCI).

Michael J. Balhoff, CFA
(410) 454-4842
mbalhoff@leggmason.com

Christopher C. King
(410) 454-5775
ccking@leggmason.com

Bradley P. Williams
(410) 454-5662
bpwilliams@leggmason.com

All relevant disclosures appear on the inside front cover of this report.

Legg Mason Wood Walker, Inc. Telecommunication Research Team

Sean P. Butson, CFA
Craig A. Mallitz
Tahmin O. Clarke

Daniel Zito
Brad Wilson

Equity Research Group

Michael J. Balhoff, CFA
Timm P. Bechter, CFA
Christopher C. King
Bradley P. Williams

Blair Levin
Rebecca Arbogast
David Kaut



Equity Research

Company Summary

Alaska Communications Systems

December 5, 2002

(ALSK-\$1.91)

TELECOMMUNICATIONS INDUSTRY

Rating: **HOLD** Risk Rating: *High*

Alaska Communications ILEC (AK)

Map Unavailable in PDF Form

Closing Price (12/4/02): \$1.91

52-Week Range: \$8-\$1

Shares Out. (mil) 30.7
Mkt. Cap. (\$mil) \$58.6
Avg. Daily Vol. (3Q02) 18,000 shares
Insider Ownership: 69%
Institutional Ownership: 24% (some insider)

FY (Dec.)	2001A	2002E	2003E
EPS (cont. ops)	(\$0.35)	(\$0.23)	\$0.01
EBITDA margin	37.8%	37.2%	41.4%
Revenue growth	5.9%	3.1%	-1.3%

Source: Company data, Legg Mason estimates, and FactSet Research Systems Inc.

Alaska Communications Systems • 600 Telephone Avenue, Anchorage, AK 99503 • Tel (907) 297-3000 • Chairman and CEO Charles E. Robinson • Web Address – www.acsalaska.com

Company Description

A public company since November 1999, Alaska Communications Systems Group (ACS) has been consolidating the Alaskan market and now serves three-fourths of the state's population with local telephone, long-distance, wireless, Internet, and data communications services. For 2001, local telephone revenues were 67% of total sales, cellular 12%, directory 10%, and long distance/data 11%, as total revenues reached \$331.7 million. At 3Q02, ACS served 327,161 access lines, 81,559 wireless subscribers, 11,045 DSL lines, and 35,614 ISP customers.

Sum of the Parts

Alaska Communications Systems ALSK			
ALSK as of Q	Estimated Value		
Asset	Multiple	Total	Share
ILEC			
Lines		inferred line	
E ILEC EBITDA	x		
ILEC EBITDA Margin			
Wireless			
PCS POPs			
Wireless Subscribers			
Other			
ISP subs			
L D customers			
DSL subs			
Fiber @ cost			
Minus net debt			
Shares			
Price @		Discount to Value	

Source: Company Data and Legg Mason Estimates

Commentary

The last couple of quarters for ALSK have reflected the ongoing negative impact on operations of the challenging regulatory and competitive environment the company continues to face in its incumbent territory, exacerbated by the weak economy. Results for 3Q02 reflected improvement over a weak second quarter, primarily benefiting from the company's efforts to control operating expenses and increasing revenues from the state of Alaska contract. We continue to be cautious about the stock in the near term as we await tangible signs of improvement on the competitive and regulatory fronts. Our rating on the shares is Hold.

Michael J. Balhoff, CFA
(410) 454-4842
mbalhoff@leggmason.com

Christopher C. King
(410) 454-5775
ccking@leggmason.com

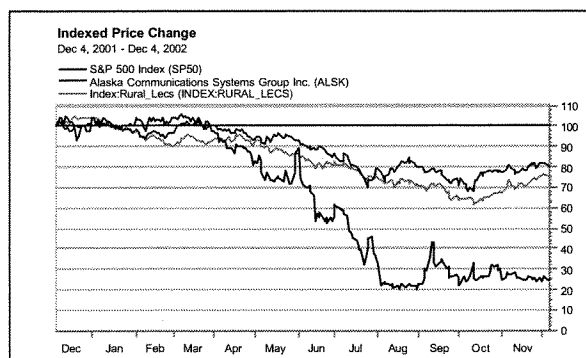
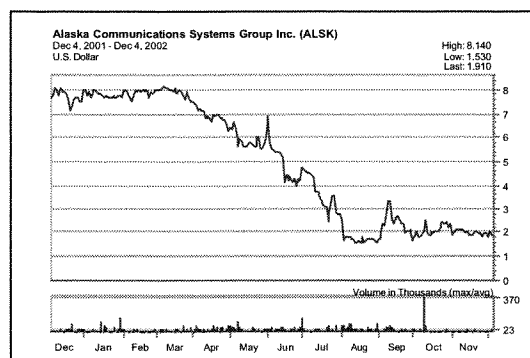
Bradley P. Williams
(410) 454-5662
bpwilliams@leggmason.com

Alaska Communications Systems Statistical Analysis									
Stock Price (12/4/02)	\$1.91				Institutional Ownership:	24.0%			
S&P 500 Price (12/4/02)	917.58				Insider Ownership:	69.0%			
Valuation Measures	1999A	2000A	2001A	2002E	Annual Growth Rates ('98-'99) ('99-'00) ('00-'01) ('01-'02)				
Company EPS	(\$0.57)	(\$0.44)	(\$0.35)	(\$0.23)	EPS	NA	NA	NA	NA
S&P 500 EPS	\$50.82	\$55.00	\$45.16	\$48.00	Sales	6.7%	4.2%	5.9%	3.1%
Company P/E	NM	NM	NM	NM	Dividends	NA	NA	NA	NA
S&P 500 P/E	18.1	16.7	20.3	19.1	Balance Sheet (\$mil.)	1999A	2000A	2001A	2002E
Relative P/E	NM	NM	NM	NM	Total debt	612.8	614.0	611.3	605.8
Book Value per share	\$7.58	\$6.69	\$6.06	\$2.13	Shareholders' Equity	248.0	215.4	191.7	67.5
Price/Book Value (x)	0.3	0.3	0.3	0.9	Debt/Total Capital	71.2%	74.0%	76.1%	90.0%
Sales (mil.)	\$300.5	\$313.1	\$331.7	\$342.0	Quarterly EPS	1999A	2000A	2001A	2002E
Market Cap./Sales (x)	0.1	0.2	0.2	0.2	First Quarter (Mar)	NA	(\$0.10)	(\$0.15)	(\$0.01) A
EBITDA (mil.)	93.8	105.2	125.3	127.2	Second Quarter (June)	NA	(\$0.08)	(\$0.09)	\$0.13 A
Market Cap./EBITDA (x)	0.5	0.6	0.5	0.5	Third Quarter (Sept)	NA	(\$0.10)	(\$0.04)	(\$0.22) A
Shares Outstanding (mil.)	23.4	32.2	31.7	31.7	Fourth Quarter (Dec)	NA	(\$0.16)	(\$0.07)	(\$0.13)
Return on Avg. Equity	NM	NM	NM	NM	Total	(\$0.57)	(\$0.44)	(\$0.35)	(\$0.23)

Alaska Communications Systems Earnings Analysis									
Income Statement (\$M except EPS)	1999A	2000A	2001A	2002E	Growth Analysis (Y-Y)				
Revenue					Local Telephone	4.7%	1.0%	1.5%	1.1%
Local Telephone	\$249.0	\$251.4	\$255.3	\$258.2	Cellular	13.5%	9.4%	2.3%	4.6%
Cellular	36.1	39.5	40.4	42.3	Interexchange network	28.9%	43.6%	62.2%	15.4%
Interexchange network, data and other	15.5	22.2	36.0	41.5	Total Revenue	6.7%	4.2%	5.9%	3.1%
Total revenue	\$300.5	\$313.1	\$331.7	\$342.0	Operating income	-23.5%	0.3%	38.8%	-2.7%
Expenses					EBITDA	-8.8%	12.0%	19.2%	1.5%
Operating expenses - local telephone	\$160.2	\$144.9	\$135.0	\$132.5	Net income	NM	NM	NM	NM
Operating expenses - cellular	24.3	24.6	24.2	26.6	EPS (continuing operations)	NA	NM	NM	NM
Operating expenses - Interexchange	22.2	33.2	47.2	55.7	Margin Analysis				
Depreciation and amortization	61.1	72.3	79.8	82.9	Operating Income	10.9%	10.5%	13.7%	13.0%
Total expenses	\$267.8	\$280.3	\$286.2	\$297.7	Depreciation and amortization	20.3%	23.1%	24.1%	24.2%
Operating income	\$32.7	\$32.8	\$45.5	\$44.3	EBITDA	31.2%	33.6%	37.8%	37.2%
Interest and other income	\$3.5	\$6.7	\$3.3	\$1.9	Cash Flow (mil.)				
Interest expense	(44.2)	(64.7)	(60.3)	(51.7)	Net income	(16.4)	(25.3)	(11.3)	(7.4)
Equity income/(loss)	(1.6)	(0.3)	0.1	-	Depreciation and amortization	61.1	72.3	79.8	82.9
Income before taxes	(\$9.5)	(\$25.5)	(\$11.4)	(\$5.6)	Capex	(74.1)	(69.1)	(87.6)	(68.2)
Tax expense/(benefit)	3.6	(0.2)	(0.1)	-	Cash dividends	NA	NA	NA	NA
Income before extraordinary item	(\$13.1)	(\$25.3)	(\$11.3)	(\$5.6)	Free cash flow	(\$29.4)	(\$22.1)	(\$19.1)	\$7.3
Extraordinary item	(\$3.3)	\$0.0	\$0.0	(\$1.8)	Telco Analysis				
Net Income (Loss)	(\$16.4)	(\$25.3)	(\$11.3)	(\$7.4)	Telco revenue per line per month	NA	\$50.48	\$49.98	\$52.49
Shares (mil.)	23.4	32.2	31.7	31.7	Operating Drivers				
Basic EPS (Continuing operations)	(\$0.57)	(\$0.44)	(\$0.35)	(\$0.23)	Access lines	325,608	329,460	332,923	324,207
Declared dividend (per share)	NA	NA	NA	NA	Total access line growth	NA	1.2%	1.1%	-2.6%
EBITDA	93.8	105.1	125.3	127.2					

Source: Company Data and Legg Mason Estimates

The information presented above summarizes Alaska Communication Systems' (ACS) combined operations for the years ended December 31, 1999. The summary information includes the combined historical results of CenturyTel's Alaska properties and Anchorage Telephone Utility (ATU) from January 1, 1999, through their acquisition date of May 14, 1999. From that point forward, the results represent ACS's consolidated operations.



Source: FactSet Research Systems Inc.

Alaska Communications Systems Group Inc.

Eric Geil, New York (1) 212-438-7833

Rationale

On Jan. 16, 2003, Standard & Poor's Ratings Services lowered its corporate credit ratings on diversified communications company Alaska Communications Systems Group Inc. and subsidiary Alaska Communications Systems Holdings Inc. (ACS) to 'BB-' from 'BB'. The downgrade is based on competitive pressure that has materially weakened ACS's business profile, impaired operating performance, and resulted in credit measures that have not met Standard & Poor's expectations for the ratings. The ratings were removed from CreditWatch, where they were placed with negative implications on July 31, 2002, over concern about credit measure weakness.

The outlook is negative.

ACS's business risk profile has declined as the company has lost local retail access lines to competition that has taken advantage of regulated low unbundled network element (UNE) loop rates in the company's key markets. Standard & Poor's is concerned that, absent regulatory changes, competitive pressure could continue to weigh on ACS and limit credit measure improvement, amid the weak economy.

The rating on ACS reflects the company's position as the leading local exchange carrier in Alaska, offset by heavy competition in the local retail access line business due to low regulatory mandated local resale loop rates to the company's local network, a narrow market with limited growth opportunities, and high acquisition and capital spending-related debt levels.

Anchorage, Alaska-based ACS offers local telephone service, wireless, long distance, data, and Internet services to business and residential customers throughout Alaska. Local telephone operations provide about two-thirds of company revenue and the bulk of cash flow. ACS had \$606 million debt as of Sept. 30, 2002.

ACS currently serves roughly 327,000 access lines in Alaska, or 68% of the state total, making it the largest local exchange carrier. However, retail lines declined 9% during the 12 months ended Sept. 30, 2002, to 241,583 lines, while lines served under lower UNE rates increased by 30.6% to 60,504 lines, eroding ACS's local revenue and profitability. Most of the decline is due to line losses to diversified communications company GCI Inc.'s competitive local exchange carrier (CLEC) business.

ACS is engaged in a number of legal and regulatory issues relating to CLEC competition and gained an interim, temporary rate increase in late 2001. However, a final regulatory decision on rates is uncertain and forthcoming, and line losses could continue to impair local revenue and profitability. One of the most pressing issues is an appeal to lift UNE rates in Anchorage, where GCI has a 40% share of access lines. In an attempt to stabilize revenues, ACS is signing up business customers to three-year discounted contracts and is bundling services. The company has also implemented cost cuts.

Revenue and profitability have also been hurt by the weak economy and expenses and delays in implementing a five-year, State of Alaska telecommunications services contract that became effective in the second quarter of 2002. The state contract is for a broad range of services and is expected to generate \$18 million in annual revenue, which should make the company's Internet services segment profitable. However, cash flow benefits from the state agreement may be insufficient to offset further erosion in the local business. Wireless and high margin directory operations provide only marginal additional cash flow diversity and offer limited growth. The unprofitable long distance segment remains a drag on the overall business.

ACS is managing to deliver modest EBITDA growth with the help of cost savings. Credit measures have improved modestly in the past year, with debt to EBITDA now below 5x. However, given unfavorable regulated rates and competitive pressure, Standard & Poor's believes further improvement may be minimal. ACS's capital spending needs are high to support business expansion and will be about \$75 million in 2002, including \$15 million to \$20 million to support the company's obligation under the State of Alaska contract.

Liquidity

ACS generates minimal discretionary cash flow. The company had \$75 million of available borrowing capacity under its revolving credit facility as of Sept. 30, 2002. Debt maturities are light through 2005, consisting of 1% annual bank principal repayments prior to required bullet repayments in 2006. Bank covenant stepdowns are moderate and offer some cushion for near-term operating weakness.

Outlook

The negative outlook reflects concern about ongoing competitive pressure that could continue to hamper ACS's operations absent any regulatory relief. Without stabilization of the local exchange business, the ratings could be lowered.

Ratings List

	To	From
Alaska Communications Systems Group Inc.		
Corporate credit rating	BB-/Negative	BB/Watch Neg
Alaska Communications Systems Holdings Inc.		
Corporate credit rating	BB-/Negative	BB/Watch Neg
Senior secured bank loan	BB-	BB/Watch Neg
Subordinated debt	B	B+/Watch Neg

Complete ratings information is available to subscribers of RatingsDirect, Standard & Poor's Web-based credit analysis system, at www.ratingsdirect.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com; under Fixed Income in the left navigation bar, select Credit Ratings Actions.

Standard & Poor's will be hosting a seminar titled, "Determining Corporate Credit Quality in a Volatile Environment," on Feb. 2-4, 2003, at the Grand Floridian Resort & Spa, Orlando, Fla. Standard & Poor's senior analysts and invited industry leaders from the corporate, banking, and investment communities will discuss trends and current issues related to corporate credit quality. For complete seminar details and registration, please call (1) 212-438-2800, or visit www.standardandpoors.com/events/CRS. You may also send an E-mail to seminars@standardandpoors.com.

		Cur	Nxt	Cur	Nxt	EBITDA	Growth
		-----	-----	-----	-----	-----	-----
EPS*	FY	NM	NM	NM	NM	NA	NA
	CY	NA	NA	NA	NA	NA	NA
GSCOPE EPS*	FY					NA	NA
	CY	NA	NA	NA	NA	NA	NA

* may differ from U.S. GAAP
=====

ESTIMATE CHANGE: REDUCING 4Q02 and 2002 & 2003 EPS ESTIMATES

We are lowering our fourth quarter EPS estimate to an \$0.11 loss from a \$0.03 loss on account of higher expected depreciation expense (ALSK indicated that depreciation expense will be approx. \$21 million in coming quarters versus our previous estimate of \$19). Including the third quarter's actual results, our new 2002 EPS estimate is a 0.21 loss (previously \$0.03 gain). In 2003, our EPS estimate is now a \$0.07 loss versus our prior estimate of \$0.05 gain. For 2003 we lowered our revenue estimate to \$345 mn from \$362 mn, with the most notable change in the local revenue segment, where we expect wholesale competition in the Juneau market to intensify. On the expense side, we are also now capturing the \$6 million of annual savings expected by ALSK for its restructuring efforts, but this only partially offsets lower EBITDA of \$133 mn (prior est. was \$139 mn) that results from weaker expected revenues next year. Also, we are now modeling depreciation expense of \$85 million, up from \$82 million previously.

RECOMMENDATION: MAINTAIN MP RATING, SLOWLY POSITIONING FOR EBITDA IMPROVEMENTS

Our MP rating on ALSK is unchanged as no real headway has been made into the leverage reduction issue and the competitive landscape in the local business continues to be pervasive. While ALSK has no serious liquidity threat in the short-term, we believe the company's lack of free cash flow prevents it from reducing its heavy debt load in 2002. However, bright spots were evident this quarter, as revenues from the State of Alaska contract hit expectations and company restructuring has streamlined operating expenses. However, better future results for ALSK hinge on improvements to the regulatory landscape. While it appears that the pendulum has swung a little in favor of the ILECs at the federal level recently, it still may be time before aggressive competition in the local market slows. Given the company's negative earnings, ALSK cannot be meaningfully compared on 2003 FCF yield or P/E valuation to its RLEC peers. On an EV/EBITDA basis, ALSK is valued at 4.8x 2003 EBITDA, a substantial discount to the 6.3x average of our other covered RLECs. We believe that this discount is warranted as heavy competition currently undermines the traditional RLEC value proposition of ALSK.

RESULTS: HIGHER THAN EXPECTED DEPRECIATION EXPENSE RESULTS IN WEAK OPERATING INCOME, BUT EBITDA WAS IN-LINE. ALSK reported an EPS loss from continued operations of \$0.22, \$0.16 below our estimate of a \$0.06 loss. Revenues of \$84.3 mn were in-line with expectations, as were cash operating expenses, driving in-line EBITDA of \$30.2 million. However, \$3.2 million of higher than expected depreciation expense as well as a \$1.8 million expense associated with restructuring contributed to a \$5 million shortfall in operating income, causing the \$0.16 miss to our estimates.

OPERATING METRICS: Competitive pressure in the local business continues to be a problem as access lines declined 1.8% year-over-year, substantially worse than the 0.5% and 0.3% declines experienced in the first two quarters of the year. While this compares favorably to the Bells, which have lost an average of 3.5% of their access lines year over year, it represents the highest annual access line decline among the RLECs which have reported 3Q02, indicating the impact of heavy competition. Meanwhile, low UNE-P rates have played a role in increased wholesale competition, as ALSK's access line mix continues to shift away from retail. Wholesale (reseller & UNE-P) lines account for 26% of ALSK's lines now compared to 22% year-end 2001. Despite the weakness in local, ALSK posted strong results in Internet and wireless. Internet revenues improved 41% sequentially (79% y-o-y), helped by 1,200 DSL adds in the quarter, bringing the customer base to over 11,000 DSL customers. Wireless revenues improved 4% year-over-year, as ALSK managed to add 452 new customers. While net adds were down, slightly higher ARPU and increased minutes of use drove the growth.

IMPLICATIONS FOR THE INDUSTRY: ALSK is probably the best example of what could happen to an ILEC in an aggressive competitive scenario. ALSK's market share in the Anchorage market has fallen close to 50%. Competitors are aware that if ALSK's market share falls below 50%, then ALSK will no longer be regulated as the dominant carrier in the market. There has been much talk about the unfriendly RBOC competitive landscape, but ALSK faces the most competitive market (Anchorage) in the country. In fact, Alaska is one, if not the only, state where regulators actually raised UNE prices (increase of \$1.07 in 4Q01). Because of the aggressive competition, ALSK plans to scale back capital spending in the competitive markets, similar to the RBOCs.

WHAT TO WATCH FOR - STATE OF ALASKA CONTRACT, LOCAL COMPETITION, AND DEBT REDUCTION REMAIN KEY ISSUES GOING FORWARD. The key to ALSK's future growth is the State of Alaska contract, where we are modeling \$18 million of revenues (down from \$20.5 mn) from the contract in 2003. ALSK seems to be on track to hit expectations following the third quarter's results when it reported \$3 million of revenues from the contract, in-line with its expectations. In the local business, competition in the Anchorage market has slowed, however, monitoring the Juneau market will be important, as competition seems to be picking up steam. Approximately half of ALSK's 2,975 new wholesale customers this quarter were located in the Juneau market. On debt reduction, ALSK likely will not generate substantial free cash flow to make any substantial strides in the fourth quarter. However, in 2003, management expects to pay down approximately \$4 million of debt.

STOCK(S) MENTIONED IN THIS RESEARCH BY TICKER

For each stock, we display the share price and the relevant disclosure code(s). Disclosure code definitions follow.

ALSK :US\$ 2.40; BC1, BC2, MM1, MM2

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GOLDMAN SACHS RATING AND PRICE TARGET HISTORY ALSK

Date	New Rating/ Target Price	Prev Rating/ Target Price	Close
07/01/2002	US\$NA	US\$12.00	US\$4.64
07/11/2001	MP	MO	US\$9.01
04/06/2001	MO	RL	US\$4.34
04/04/2001	RL	MO	US\$4.63
04/04/2001	MO	RL	US\$4.63
04/04/2001	US\$12.00	US\$25.00	US\$4.19

11/23/1999	RL	NR	US\$14.00
11/23/1999	US\$25.00	US\$NA	US\$14.81

Telecommunications Services

Industry Report

Frank G. Louthan IV
 (727) 575-5586
 flouthan@ecm.rjf.com
 Ben Gordon, Res. Assoc.

**EQUITY
 RESEARCH**

January 28, 2003

The ILEC Industry: Defensible Markets Create Defensive Stocks



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ILEC Key Investment Points

Incumbent Status Offers Defensible Market

We believe the Incumbent Local Exchange Carriers (ILECs) enjoy a competitive advantage due to their natural monopoly position within legacy markets. Incumbency provides immediate access to a relatively captive customer base to which additional products and services can be sold, and has been a significant deterrent to competition, in our opinion.

Strong Cash Flow Offers Flexibility

The ILECs' ability to generate strong, stable cash flow from their legacy access lines is a competitive advantage relative to newer telecom operators, in our opinion. Strong cash flow allows the ILECs to self-fund growth and expansion projects. We view the sector's ability to service and pay down debt as very valuable considering the capital-intensive nature of the industry, and investors' aversion to the debt-laden disasters in other areas of telecom over the past few years.

Defensive Play on the Economy

In our opinion, the ILECs' residential customer base is not likely to disconnect their phones due to a weak economy and even Internet and additional services have become a staple of the average consumer's life. As a result, we believe ILECs' results should be less affected by a prolonged economic downturn, as residential customers represent a steady, recurring revenue and earnings stream.

Favorable Regulatory Environment

We believe the ILECs' competitive position is reinforced through favorable regulation. The benefits of regulation include protection from competitors, and access to certain subsidies available to carriers providing services to rural and suburban markets. We view these advantages as key reasons to expect the ILECs should maintain market share. With less exposure to UNE-P and wireless replacement, we believe the ILECs will continue to demonstrate positive results as the larger RBOCs are faced with fundamental competitive pressures.

Capitalizing on Growth Prospects

From access line aggregation to edge-out CLEC to data and Internet access, we believe the ILECs continue to have opportunities to drive incremental growth and expand their margins. We believe these factors, combined with additional opportunities for new investment, will drive higher levels of ILEC revenue and EBITDA over the next few years, with less overall risk relative to pure-play carriers.

Alaska Communications

(ALSK:NASDAQ)

Not Rated

Alaska Communications Services (ACS) currently serves 327,000 access lines in the state of Alaska, and is the largest local telephone provider in the state. Additionally, the company has about 82,000 wireless subscribers, and offers a wide range of local, long distance, and Internet and data products. The company has recently expanded its Internet products to utilize its recently completed statewide IP network. ACS is headquartered in Anchorage, Alaska, and employs approximately 1,000 people.

Current Price \$2.38

- ◆ **Largest provider in Alaska.** We estimate the company has about 75% of its population covered by its local telephone network. Its services include local, long distance, wireless, and data services. The company's local exchanges are concentrated in and around Juneau, Anchorage, and Fairbanks, Alaska. The company is currently experiencing positive top-line trends, with revenue growth of 5.3% YTD in 2002.

Shares Out. (mil.) 31.653
Market Cap. (mil.) \$73.7
LT Debt (mil.)/% Cap. \$600.8/89.3%

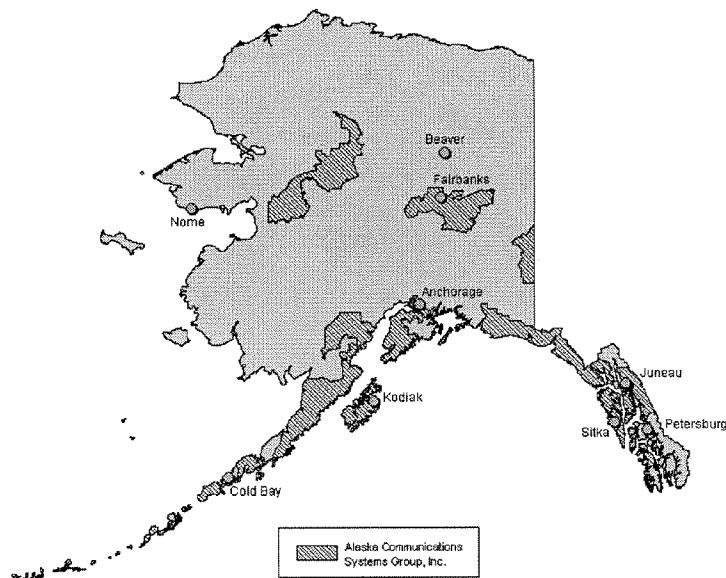
Revenues (mil.)

2000A \$313.0
2001A \$331.7
2002 YTD \$259.2

EBITDA (mil.)

2000A \$111.6
2001A \$128.7
2002 YTD \$97.4

- ◆ **Competitive situation very challenging.** ACS currently faces a significantly challenging regulatory environment, with notable inroads having been made by competitor General Communications (GNCMA/\$6.42). We estimate General has taken 60,500 access lines, primarily on a UNE-L basis. The ACS UNE rate of \$14.92 in Anchorage (ACS's largest competitive market) seems low, particularly considering a lack of de-averaging zones in the state. We believe this has put a significant burden on the operations of ACS, and any positive changes regarding the regulatory structure in Alaska would be very beneficial for ACS shareholders.
- ◆ **IP Network Offers Growth.** The company recently completed a statewide IP network, which we believe offers significant private line and long-haul transport opportunities. The company has already placed significant customers on the network, including the state government, and we believe this unregulated aspect of the business will continue to offset competitive losses due to demand for advanced services.
- ◆ **Wireless Operations.** The company is currently the largest wireless provider in the state, with approximately 82,000 subs and about 470,000 covered Pops. We view wireless as an important service offering, particularly due to the remote nature of the state and the demand for communications. We also view the company's penetration into the North Slope oilfields as a strong asset, as this takes advantage of heavy business and seasonal demand. The company is migrating its TDMA platform to CDMA.
- ◆ **Management team.** The company has a strong and deep management team that has extensive experience in the telecommunications industry, and Alaska in particular. **Charles E. (Chuck) Robinson** is chairman and CEO of ACS and has attained numerous achievements in operational and management roles for the telecommunications businesses serving in Alaska since 1957. **Wesley E. Carson** is president and COO of ACS, having served in the telecommunications industry since 1980, and holds a BA from Brigham Young University, a Masters degree from the University of Illinois-Springfield, and a Juris Doctor degree from Georgetown University. **Kevin P. Hemenway** is Treasurer and Chief Financial Officer for ACS, and has served in the position since November 2000. He formerly worked as Chief Financial Officer for Atlantic Tele-Network, Inc.; a Virgin Islands-based telecom company.



Source: Raymond James, Map Info, and company reports.